

Private foundations; qualifying distribution; contribution to other private foundation. An amount contributed by a private foundation to another private foundation that, in the taxable year following the taxable year in which it received the contribution, established an approved set-aside in the amount of the contribution and made a valid election to treat the entire amount of the set-aside as a distribution out of corpus may be treated by the donor foundation as a qualifying distribution under section 4942 of the Code.

'Advice has been requested whether, under the circumstances described below, amounts contributed to a private foundation by another private foundation may be treated as qualifying distributions by the donor under section 4942 of the Internal Revenue Code of 1954.

'Foundation M and Foundation Y are both private foundations described in section 501(c)(3) of the Code. Foundation M is on a calendar year basis and Foundation Y has a fiscal year ending July 31. On February 1, 1976, Foundation M made a contribution of x dollars to Foundation Y.

'On September 15, 1975, Foundation Y made distributions equal to its distributable amount for its prior year. During the same month, it also applied for and received approval for a set-aside pursuant to section 4942(g)(2) of the Code for its fiscal year ending July 31, 1977. On October 15, 1976, Foundation Y entered a set-aside of x dollars on its books and records as an obligation to be paid out and made a timely election to treat the entire amount as a distribution out of corpus.

'Section 4942(g)(1) of the Code provides that the term 'qualifying distribution' means any amount paid to accomplish one or more purposes described in section 170(c)(2)(B), other than any contribution to (i) an organization controlled (directly or indirectly) by the foundation or one or more disqualified persons (as defined in section 4946) with respect to the foundation, except as provided in section 4942(g)(3), or (ii) a private foundation which is not an operating foundation (as defined in section 4942(j)(3)), except as provided in section 4942(g)(3), or any amount paid to acquire an asset used (or held for use) directly in carrying out one or more purposes described in section 170(c)(2)(B).

'Section 4942(g)(3) of the Code provides that the term 'qualifying distribution' includes a contribution to a section 501(c)(3) organization described in section 4942(g)(1)(A) if-

(A) not later than the close of the first taxable year after its taxable year in which such contribution is received, such organization makes a distribution equal to the amount

of such contribution and such distribution is a qualifying distribution (within the meaning of paragraph (1) or (2), without regard to this paragraph) which is treated under subsection (h) as a distribution out of corpus (or would be so treated if such section 501(c)(3) organization were a private foundation which is not an operating foundation), and

(B) the private foundation making the contribution obtains adequate records or other sufficient evidence from such organization showing that the qualifying distribution described in subparagraph (A) has been made by such organization.

'Section 4942(h)(1) of the Code provides that any qualifying distribution made during a taxable year shall be treated as made first out of the undistributed income of the immediately preceding taxable year, second out of the undistributed income of the current taxable year, and then out of corpus. Where a qualifying distribution is not treated as made out of the undistributed income of the immediately preceding taxable year, section 4942(h)(2) and the regulations thereunder provide that the foundation may elect to treat any portion of such distribution as made out of the undistributed income of a designated prior taxable year or out of corpus.

'Foundation M, therefore, has made a qualifying distribution for its calendar year ending December 31, 1976, only to the extent that Foundation Y meets two requirements; first, Foundation Y must itself make a qualifying distribution within the taxable year after its receipt and, second, that distribution must be treated as a distribution out of corpus.

'With respect to the first requirement, Foundation Y has an approved set-aside. Amounts set aside pursuant to that approval are qualifying distributions. Therefore, Foundation Y has made a qualifying distribution in the amount of x dollars in the year following its receipt.

'With respect to the second requirement, Foundation Y has made distributions equal to the distributable amount for its prior year, plus x dollars. Section 4942(h) of the Code treats qualifying distributions as made first out of the undistributed income of the immediately preceding taxable year. Since Foundation Y had no undistributed income for its prior year at the time it set aside x dollars, no amount of the x dollars is treated as a distribution out of undistributed income of the prior year.

'Section 4942(h) of the Code next treats qualifying distributions as made out of the undistributed income of the current taxable year. However, such amount may be treated as a distribution out of the undistributed income of a designated prior taxable year or out of corpus if a timely election is made.

Since Foundation Y made a timely election, the entire amount of x dollars is treated as a distribution out of corpus.

'Accordingly, since Foundation Y has made a qualifying distribution in the amount of x dollars in the year following its receipt, and such amount is treated as a distribution out of corpus, Foundation M has made a qualifying distribution in that amount.